

***United States Court of Appeals
for the Second Circuit***



APPELLEE'S BRIEF

77-6122

Signed

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

CHARLES LUBUS, Jr.,

Plaintiff-Appellant

v.

UNITED STATES OF AMERICA,

Defendant-Appellee

ON APPEAL FROM THE JUDGMENT OF THE
UNITED STATES DISTRICT COURT FOR THE
DISTRICT OF CONNECTICUT

BRIEF FOR THE APPELLEE

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STATEMENT OF THE ISSUE PRESENTED

Whether the District Court correctly ruled that items of tax preference covered by Sections 56 through 58 of the Internal Revenue Code of 1954 in amounts less than the exempt amount are subject to the minimum tax imposed by Section 56 in addition to, and not in lieu of, the normal income taxes imposed.

STATEMENT OF THE CASE

This is an action for refund of \$2,638.85 of income taxes for 1973 through 1975. (Compl.^{1/}) Taxpayer filed a claim for refund, which was disallowed by the Internal Revenue Service. Taxpayer

1/ Taxpayer has submitted only copies of the District Court's Memorandum of Decision and Judgment as his appendix. References are to the original record on appeal.

thereafter instituted this suit in the United States District Court for the District of Connecticut. (Compl.) The United States filed a motion for judgment on the pleadings for failure to state a cause of action which was granted by the District Court (Judge Newman). (Memorandum of Decision and Judgment.) Judgment was entered on August 2, 1977. Taxpayer filed a timely notice of appeal on August 5, 1977. This Court has jurisdiction pursuant to 28 U.S.C., Section 1291.

Taxpayer maintains that Sections 56 through 58 of the Internal Revenue Code of 1954, which relate to the minimum tax for specified tax preferences, are the only provisions of the Code which tax preference items, i.e., interest income, dividends, rents, royalties and capital gain and, further, that that tax is imposed only when the total of these items exceeds, for the years in question, \$30,000. On this theory, taxpayer seeks refunds of \$836.84, \$1,012.94 and \$789.07 for the years 1973, 1974 and 1975, respectively. (Compl.) The District Court dismissed taxpayer's complaint as frivolous (Memorandum of Decision) and this appeal followed.

SUMMARY OF ARGUMENT

Section 56 of the Internal Revenue Code imposes a tax on certain tax preference items (in excess of an exempt amount) and as the statute sets forth in clear and unambiguous language, this tax is in addition to, and not in lieu of other taxes. Taxpayer's contrary assertion that the minimum tax is in lieu of the income tax up to the exempt amount ignores this plain language and consequently, his contention is clearly erroneous. Moreover, the items of income--rents, royalties, dividends, interest and all capital gains--which taxpayer asserts are subject only to the tax in tax preferences, are not even tax preference items as defined in Code Section 57. Taxpayer's argument is wholly without merit and the District Court's decision should therefore be affirmed.

ARGUMENT

THE DISTRICT COURT CORRECTLY RULED THAT THE TAX IMPOSED BY SECTION 56 OF THE INTERNAL REVENUE CODE IS IN ADDITION TO, AND NOT IN LIEU OF, OTHER TAXES IMPOSED

Taxpayer's contention that the minimum tax on tax preference items is in lieu of, rather than in addition to, the normal income tax for the first \$30,000 of such items is wholly without merit. Secondly, taxpayer erroneously argues that rents, royalties, dividends and interest and all capital gains are items of tax preference as defined in Section 57 of the Internal Revenue Code of 1954, Appendix, infra.

The minimum tax provisions were added by Section 301(a) of the Tax Reform Act of 1969, P.L. 91-172, 83 Stat. 487, and consist of Sections 56, 57 and 58 of the Code. Section 56, Appendix, infra, imposes a tax of 10 percent on the amount by which the tax preference items (defined in Section 57) in excess of \$30,000^{2/} exceed the taxes imposed by Chapter 1 of the Internal Revenue Code (which includes the income tax), reduced by certain credits. Section 56(a) explicitly states that the tax imposed by that section is "In addition to the other taxes imposed by this chapter * * *." The chapter to which it refers is Chapter 1 of the Internal Revenue Code.

^{2/} Section 56 was amended by Sec. 301(a) of the Tax Reform Act of 1976, P.L. 94-455, 90 Stat. 1520, to increase the rate of tax to 15 percent and decrease the amount of items of tax preference exempted from the minimum tax to \$10,000.

Chapter 1 of the Code, relating to normal taxes and surtaxes, includes Section 1, which imposes a tax on the taxable income of individuals.

It is a well settled principle that the words of statutes--including revenue statutes--should be interpreted in their ordinary, everyday sense. Crane v. Commissioner, 331 U.S. 1, 6 (1947); Old Colony R. Co. v. Commissioner, 284 U.S. 552, 560 (1932). There can be no question here that Section 56, which is plain on its face, imposes in clear and unambiguous language a tax in addition to the tax imposed by Section 1. Taxpayer's brief, consisting of less than one page, contains no hint of support for his interpretation of the statute, which is plainly contrary to the statutory language.

Although language as clear as the language of Section 56(a) does not require recourse to the legislative history, a brief review of that history shows beyond peradventure that the statute says what Congress intended it to say. Congress was particularly concerned that individuals who earned substantial incomes were able to avoid taxation in large part or altogether by structuring their affairs so as to take maximum advantage of certain deductions in the form of tax shelters. See S. Rep. No. 91-552, 91st Cong., 1st Sess., pp. 111-118 (1969-3 Cum. Bull. 423, 495-499). Sections

56 through 58 were thus intended to impose tax on high-income individuals who otherwise unjustly avoided tax. The \$30,000 exemption represents a Congressional policy decision (at that time), that only preference items in excess of that amount should be subject to the additional tax.

The Tax Court has also noted that the minimum tax was designed to insure that the tax preference items were subject to some minimal tax. In holding that the tax imposed by Section 56 was not eligible for income averaging (Code Sections 1301 through 1305), the Tax Court concluded that the minimum tax was a separate, "self-contained unit of taxation." Riley v. Commissioner, 66 T.C. 141, 144 (1976).

Taxpayer is confused as to what items are tax preference items. Section 57 sets forth the items which constitute tax preference items. Generally, these items are items such as accelerated depreciation which allow taxpayers to claim deductions in excess of real economic costs, or items such as long-term capital gain, which may reduce the tax recognition of gain

below real economic gain. Taxpayer, however, erroneously asserts that "all Interest Income, Dividends, Rents, Royalties, and Capital Gains" (Br.) are subject to the minimum tax.

Section 57 does not include the above-enumerated items, other than capital gains, and then only to the extent of one half, and not all, of the net long-term capital gains over the net short-term capital losses. Sec. 57(a)(^{3/}9).

The source of taxpayer's contention that the other items are tax preference items is even more obscure. The only possible source for this contention is Section 57(b)(a)(B)(i) prior to its amendment by Section 301(c)(2) of the Tax Reform Act of 1976, P.L. 497, 94-450, 90 Stat. 1520. This section formerly defined "investment income" as "gross income from interest, dividends, rents, and royalties." But, this definition was only used to calculate the net investment income (Sec. 57(b)(2)(A)) which in turn is used to determine excess investment interest which was a tax preference item formerly described in Section 57(a)(1).

^{3/} This is, of course, that amount of capital gains which is deductible under Section 1202, and is therefore an amount which would not otherwise be taxed under Section 1 of the Code. The other half of net long-term capital gains would, of course, be taken into account in computing taxable income.

Thus, the item included as a tax preference item was not interest, dividend, rent or royalties, but the excess of interest paid on indebtedness used to enter into the production of interest, etc., in excess of the net return, on the investment itself.

Taxpayer's contention that the first \$30,000 of tax preference items is exempt from income tax is clearly erroneous, as is his contention that the items on which he bases his claims are even tax preference items. The District Court correctly dismissed this suit as frivolous.

CONCLUSION

For the reasons set forth above, the judgment of the District Court should be affirmed.

Respectfully submitted,

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NOVEMBER, 1977.

CERTIFICATE OF SERVICE

It is hereby certified that service of this brief has been made on appellant, appearing pro se, by mailing four copies thereof on this 30th day of November, 1977, in an envelope, with postage prepaid, properly addressed to him as follows:

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Internal Revenue Code of 1954 (26 U.S.C.):

SEC. 56 [as added by Sec. 301(a), Tax Reform Act of 1969, P.L. 91-172, 83 Stat. 487, and amended by Sec. 501(a)(1), Excise, Estate and Gift Tax Adjustment Act of 1970, P.L. 91-614, 84 Stat. 1836; Sec. 601(c)(4), Revenue Act of 1971, P.L. 92-178, 85 Stat. 497; Secs. 2002(g)(4) and 2005(c)(7), Employee Retirement Income Security Act of 1974, P.L. 93-406, 88 Stat. 829; and Secs. 203(b)(2) and 208(d)(2), Tax Reduction Act of 1975, P.L. 94-12, 89 Stat. 26] 4/. IMPOSITION OF TAX.

(a) In General.--In addition to the other taxes imposed by this chapter, there is hereby imposed for each taxable year, with respect to the income of every person, a tax equal to 10 percent of the amount (if any) by which--

(1) the sum of the items of tax preference in excess of \$30,000, is greater than

(2) the sum of--

(A) the taxes imposed by this chapter for the taxable year (computed without regard to this part and without regard to the taxes imposed by sections 408(f), 402(e), 531, and 541) reduced by the sum of the credits allowable under--

(i) section 33 (relating to foreign tax credit),

(ii) section 37 (relating to retirement income),

(iii) section 38 (relating to investment credit),

(iv) section 40 (relating to expenses of work incentive program), and

(v) section 41 (relating to contributions to candidates for public office);

(vi) section 42 (relating to credit for personal exemptions),

(vii) section 44 (relating to credit for purchase of principal residence; and

(B) the tax carry overs to the taxable year.

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4/ The amendments made in 1974 and 1975, adding the references to Sections 408(f) and 402(e) in Section 56(a)(2)(A) and adding subsections (vi) and (vii) to that section, apply to only part of the taxable period here involved.

SEC. 57. [as added by Sec. 301(a), Tax Reform Act of 1969,
supra]. ITEMS OF TAX PREFERENCE.

(a) In General.-- For purposes of this part, the items, of
tax preference are--

(1) Excess investment interest.--The amount of the
excess investment interest for the taxable year (as determined
under subsection (b)).

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(9) Capital gains.--

(A) Individuals.--In the case of a taxpayer other
than a corporation, an amount equal to one-half of the
amount by which the net long-term capital gain exceeds
the net short-term capital loss for the taxable year.

(B) Corporations.--In the case of a corporation,
if the net long-term capital gain exceeds the net short-
term capital loss for the taxable year, an amount equal
to the product obtained by multiplying such excess by
a fraction the numerator of which is the sum of the normal
tax rate and the surtax rate under section 11, minus the
alternative tax rate under section 1201(a), for the taxable
year, and the denominator of which is the sum of the normal
tax rate and the surtax rate under section 11 for the
taxable year. In the case of a corporation to which
section 1201(a) does not apply, the amount under this sub-
paragraph shall be determined under regulations prescribed
by the Secretary or his delegate in a manner consistent with
the preceding sentence.

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